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Audit Report

Audit Services

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EMPLOYMENT SECURITY DEPARTMENT

Agency No. 540

July 1, 1996 Through June 30, 1997

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EMPLOYMENT SECURITY DEPARTMENT
Agency No. 540
July 1, 1996 Through June 30, 1997

Overview

We have conducted an annual audit of the Employment Security Department for the year ended June 30, 1997. Generally, the scope of our audit will encompass financial transactions, federal programs, and tests of compliance with state laws and regulations as required by *Revised Code of Washington* 43.09.260. The primary areas examined during an audit are those representing the highest risk of noncompliance, misappropriation or misuse. Other areas are reviewed on a rotating basis over the course of several audits.

Depending on the size of an entity's financial account balances, we perform certain procedures to express an opinion on the general purpose financial statements of the state of Washington. Our opinion on the state's financial statements is provided in the Washington State Comprehensive Annual Financial Report. The scope of our audit of the Employment Security Department included procedures related to our financial statement opinion.

In accordance with the Single Audit Act Amendments of 1996, we annually audit major federal programs administered by the state of Washington. Depending on the size and risk associated with an agency's federal programs, we perform certain procedures to evaluate the state's internal controls and compliance with federal requirements. Rather than perform a single audit at each agency, we audit the state as a whole, and publish the results in a statewide single audit report. The work performed at the Employment Security Department included procedures to satisfy the requirements of the 1997 statewide single audit.

There were findings, which are listed in the Schedule of Findings following this Overview, for the Employment Security Department. Findings 1, 3 and 4 will also be reported in our 1997 statewide single audit report.

BRIAN SONNTAG, CGFM
STATE AUDITOR

March 4, 1998

EMPLOYMENT SECURITY DEPARTMENT
Agency No. 540
July 1, 1996 Through June 30, 1997

Schedule Of Findings

1. The Employment Security Department does not have adequate controls over cash receipts.

Description of Condition

Our examination of three Employment Security Department (ESD) headquarters units, Treasurer's Unit, Benefit Payment Control Unit (BPC), Employer Accounts Unit (TAX) and various field offices revealed weaknesses in controls over the handling and completeness of cash receipts. Our testing found that approximately \$868,000 is processed through these units and offices per week. The following conditions were noted:

- Segregation of duties is inadequate. Employees responsible for receiving cash also make bank deposits, post payments and make adjustments to the accounts receivable system.
- No log is prepared for cash receipts received in the mail. This results in a lack of accountability, especially when receipts are then informally processed by multiple employees before being deposited.
- There is no reconciliation between cash received and the entries made to accounts receivable in the GUIDE (General Unemployment Insurance Design Effort) system or employer accounts in the TAXIS (Tax Information System) system. We were unable to account for \$49,629 in credits to the accounts receivable balances made by the BPC unit during a four-day period. Also, we found 20 cash receipts deposited during the same period which were never credited to the accounts receivable balances.
- Cash receipts are not properly secured.
- Checks are not restrictively endorsed immediately upon receipt. Restrictive endorsements ensure that checks will be deposited only to agency accounts.
- Manual cash receipt books are not adequately safeguarded and accounted for.
- Cash receipts are not deposited intact on a daily basis. We found that funds received on a given day were not consistently deposited completely on the day of receipt.

Cause of Condition

Procedures over cash receipting did not receive adequate administrative attention as the agency implemented a major new computer system, GUIDE. The implementation of this system had a major affect on the cash receipting processes at ESD. There were shifts in responsibilities, functions, and workloads of various agency units and employees. In many cases these changes affected division of duties between employees handling cash and performing other functions. We also found that the agency policy over cash receipting does not adequately address control procedures established by the Office of Financial Management (OFM) to ensure adequate safeguarding of cash.

Effect of Condition

Lack of adequate control procedures over cash receipts increases the risk that errors, irregularities, or theft could occur and not be detected.

Recommendations

- Segregate the duties of receipting, posting and depositing of cash receipts.
- Implement the use of cash logs and transmittals to establish accountability when cash is received or transferred between staff members or units.
- Reconcile entries made to accounts receivable and employer accounts with the cash receipts deposited. In addition, require approval and review of account adjustments.
- Ensure cash receipts are properly secured.
- Ensure that cash receipts are deposited intact on a daily basis.
- Restrictively endorse checks immediately upon receipt.
- Establish suspense accounts for receipts of overpayments and monitor the accounts.
- Update the agency's cash receipting policy to reflect compliance with OFM requirements.

Agency's Response

In addressing this finding the agency has taken the following actions:

1. *To resolve the issue of inadequate segregation of duties, keying of payments on Unemployment Insurance (UI) benefit overpayments and employer tax accounts receivable will be performed by staff not responsible for the cash receipting function. Funding for additional staff has been allocated in the UI Division to perform this input to ensure adequate segregation of duties occurs.*

2. *Cash logs will be maintained by the Treasurer's and Benefit Payment Control Units for cash received through the mail on UI benefit overpayment receivables. This provides for better accountability for cash received by these units.*
3. *As the Treasurer's Unit will no longer be keying payments to accounts receivable, the unit will reconcile daily cash they have processed with accounts receivable input totals provided by the UI Division (Employer Tax and Benefit Payment Control Units).*
4. *Additional resources have been allocated to ensure that mail received in the Employer Tax mailroom will be opened by two people. These employees will not have the ability to post to the Employer Tax accounts receivable. A cash log for the majority of Employer Tax payments already exists. With the purchase of a copy machine for the Employer Tax mailroom, checks received, for which sufficient account information is not available, will no longer need to leave the area for identification of account numbers. Policy will be to require the return of the necessary information the same day. These new procedures will allow verification, logging and deposit of all cash within 24 hours of receipt. The additional staff and copy machine will be in place by June 30, 1998. A long-term resolution for Employer Tax receipts is being worked on with the development of an imaging system for scanning, storing and retrieving UI Tax information, including all checks received.*
5. *Exceptions noted by the State Auditor's Office in posting to benefit overpayment accounts receivable have been corrected. Accounts for which improper credit was given have had the credits reversed. Conversely, accounts for which cash had been received but for which credit had not been given have been credited. The issue of depositing receipts but not crediting payments to the accounts receivable balance will be eliminated when the GUIDE system's suspense file is operational. The suspense file has been given priority and should be functional within the next six to nine months. In the interim, additional manual reviews and safeguards have been implemented to ensure payments are properly credited to accounts.*
6. *The Employer Tax Unit will reconcile credits to employer accounts and cash receipts by ensuring that batch tapes (employer account credits) are totaled prior to deposit of cash with the Treasurer's Unit. These batch tape totals will be verified against the returned total from the Treasurer's Unit. Batch tapes will be verified against the credits to individual accounts through daily input detail listings and against an independent on-line review of on-line transactions and log.*
7. *A secured area has been requested for processing cash receipts.*
8. *The Treasury Unit will write and implement new procedures to properly account for and safeguard manual cash receipt books.*
9. *Cash receipts in the Benefit Payment Control Unit will be entered on the daily cash log and checks will be restrictively endorsed at the time the mail is opened. The Treasury Unit will review unit procedures and endorsing machine operations to ensure compliance with endorsement requirements.*

10. *Issues addressed in this audit finding which relate to field offices will be shared with staff responsible for cash receipting functions. Training on cash receipting policies and procedures will be provided if necessary.*

Auditor's Remarks

We appreciate the agency's commitment to strengthening controls over cash receipts. We will review the corrective action during our next regular audit.

Applicable Laws and Regulations

The state of Washington Office of Financial Management (OFM) *Policies, Regulations, and Procedures* manual prescribes the following:

Section 6.2.2.1.1:

- a. Division of duties in handling of cash is one of the most effective ways to ensure control over this asset. No individual is to have complete control in the handling of cash. Specifically, there is to be a separation of duties in the actual handling of money, recording the transactions, and reconciling bank accounts.
- b. Incoming cash is to be made a matter of record as soon as possible.
- c. Mail is to be opened by two persons. Remittances by mail are to be listed in duplicate at the time the mail is opened. The listing is to be periodically compared with the deposit by a third person.
- e. A secure area for the processing and safeguarding of cash received is to be provided. Access to the secured area is to be restricted to authorized personnel only. The secured area is to be locked when not occupied.
- i. When cash is received in branch offices, it is to be transmitted to the central office through the banking system.
- k. Receipts are to be deposited intact on a daily basis.
- m. A person other than the cashier or receivable bookkeeper is to make the bank deposit.

Section 2.2.4.1.4.a:

- (1) Daily, cash is to be counted and reconciled with the appropriate records reflecting the day's transactions.

Section 6.2.2.1.8:

- e. Credit adjustments to receivable balances are to be approved by officials not involved in the collection activity.

Other sections in the OFM *Policies, Regulations, and Procedures* manual that address cash receipting procedures include Sections 2.2.2.1.1, 2.2.4.3.5 and 6.1.1.2.4.

- 2. The Employment Security Department does not have adequate internal controls over the vendor payment process.

Description of Condition

Our audit of vendor payment procedures at nine Employment Security Department (ESD) field offices and at the headquarters vendor payment unit in Olympia found the following weaknesses:

- Data input documentation is not consistently reconciled with data output, and the reconciliations are performed by the same person who input the payment. At the headquarters vendor payment unit, staff who perform the reconciliations also receive and mail the warrants. Adequate segregation of duties ensures that agency payments are accurate and authorized.
- Payments are processed by the vendor payment unit without adequate verification of approval signatures. In addition, some payments are processed with no approval signatures.

Cause of Condition

An independent input/output reconciliation is not performed at the vendor payment unit because headquarter staff assumed field staff were responsible for performing the reconciliations. However, our testing at the field offices found that such reconciliations are not always performed or were not performed by someone independent of the payment process. Vendor payment staff also indicated they are unable to verify whether approval signatures are appropriate because of the volume of employees authorized to approve various agency expenditures.

Effect of Condition

Weak internal controls over vendor payments has resulted in fraudulent payments being processed at the Lewis County Job Service Center. This condition was investigated and reported by the United States Department of Labor, Office of Inspector General. Current lack of adequate controls increases the risk of other inappropriate payments being made without detection.

Recommendations

- Payment transaction output should be compared with source documents by staff independent of the transaction processing.
- Duties between inputting payments and mailing warrants should be segregated.

- Only transactions with evidence of verified payment approval signatures should be processed.

Agency's Response

The agency has taken the following actions to address issues identified in the finding:

1. *Procedures in the headquarters vendor payment unit have been changed to provide better internal control. One person performs reconciliation, i.e., balances the warrant register against the batch balances to ensure that warrant amounts are correct. A different person mails the warrants.*
2. *Employees in the vendor payment unit have been reminded that the presence of an original approval signature is mandatory. Invoices lacking this information must be returned to the originating cost center. In addition, the supervisor of the unit conducts spot checks of the batches to determine that invoices are being properly approved and paid. Included in this review is a spot check for batch approval.*
3. *To improve our ability to determine who has approval authority, we have asked the cost centers in the agency to prepare a list of persons who have approval authority. The original list is to be kept on file in the cost center for review by auditors or other appropriate people. In addition, a copy is to be sent to the Fiscal Office to use as a comparison document should we have questions about a particular invoice. Cost centers will be asked to update the information on an annual basis.*
4. *Agency field offices identified in this finding have revised their payment processing to ensure proper approval of invoices occurs prior to submission to the headquarters Vendor Payments Unit or on-site direct system input. In addition, reconciliation of cost center expenditures will be performed by staff not involved in the invoice approval or input process.*

Auditor's Remarks

We appreciate the agency's commitment to strengthening controls over the vendor payment process. We will review the corrective action during our next regular audit.

Applicable Laws and Regulations

The state of Washington Office of Financial Management's *Financial and Administrative Policies, Regulations, and Procedures* manual prescribes the following:

Section 6.2.2.1.11.d:

Controls are to be established over completeness and accuracy of input, processing and output.

Section 6.2.2.1.3.f(5):

The recording of disbursements. To the extent possible, employee duties in this area are to be complementary to or checked by another employee.

Section 6.2.2.1.3.g:

Each cash disbursement is to be properly vouchered and approved by the proper authorities of the agency before the actual disbursement occurs. This will ensure the proper and regular review of all disbursements.

3. The Employment Security Department does not have adequate controls over access to the Financial Accounting and Reporting System and the JOBS Financial System.

Description of Condition

Our review of access controls for the Financial Accounting and Reporting System (FARS) and the JOBS Financial System (JFS) at the Employment Security Department (ESD) revealed the following weaknesses:

- Individuals with access were no longer employed by ESD, or had moved to different offices.
- Individuals having access to payroll and vendor payment screens no longer performed the input activity for these functions.
- Individuals in supervisory positions have input capability.

Cause of Condition

Weaknesses concerning access to FARS and JFS are due to the lack of a formal policy and procedure to change access within the system as employees change positions or leave the agency. Weaknesses concerning access to FARS were noted in the *State of Washington Statewide Single Audit Report*, for fiscal years 1994, 1995, and 1996. Weaknesses relating to JFS access were noted in fiscal years 1995 and 1996.

Effect of Condition

Lack of adequate controls over system access increases the risk that errors or irregularities could occur and not be detected. In addition, if such conditions occurred they could have an effect on federal grant funds processed through these systems.

Recommendations

- Review the existing FARS and JFS access listing for individuals no longer requiring access to the system and remove their access.
- Institute a procedure for removing access as individuals leave the agency or move to different offices within the agency.

Agency's Response

The agency's Office of Information Services (OIS) continually strives to provide better information so the local managers can perform their role in safeguarding agency resources against unauthorized access. In addressing system access issues related to this finding, OIS has taken the following steps:

- 1. The agency's policy on Mainframe Automated Systems Security was updated to clearly specify the responsibility of managers to assign appropriate system access and ensure it continues to be appropriate. Any change in employee job duties or status that results in a different need for mainframe security access must be reported to OIS.*
- 2. A process has been developed by OIS to identify staff who have left the agency or changed cost centers and have access to agency systems. OIS Production Control revokes the user's logon and removes their ability to access agency-controlled systems. The user is subsequently deleted once written authorization is received from the responsible manager or the logon has been inactive for six months.*
- 3. OIS produces a Security Authorization Report that is distributed to authorized ESD managers on a monthly basis. The report shows employee system access information for all systems including FARS and the JOBS Financial System (JFS). This report identifies employees having access to these systems as well as the profile or model assigned. The profile or model outlines the specific system functions the employee is authorized to perform. The report now enables managers to evaluate the propriety of their employee's system access.*
- 4. OIS Production Control has created an on-line system that enables the local managers and security designees to review security information on-line. This process allows managers to view and update their employee's access at any time during the month.*
- 5. OIS plans to issue detailed instructions to managers for reviewing the Security Authorization Report. These instructions will accompany the June 1998 version of the report.*

In addition, issues with staff having inappropriate or questionable access, as identified by SAO during their audit, have been resolved. Supervisory employees and staff not performing payroll or vendor payment input have had this access removed. To prevent future exceptions, the agency has assembled a task team to develop an off-payroll form for cost center managers to complete for staff leaving the agency to ensure system access is terminated.

Auditor's Remarks

We appreciate the agency's commitment to strengthening controls over access to agency systems. We will review the corrective action during our next regular audit.

Applicable Laws and Regulations

The state of Washington Office of Financial Management's *Financial and Administrative Policies, Regulations, and Procedures* manual prescribes the following:

Section 6.2.2.1.11.j:

Controls are to be in place which safeguard and limit access to data processing equipment, tapes, disks, files, system documentation, and application program documentation to authorized employees.

Section 6.1.1.2.4.b.(1):

Division of Duties - Whenever possible, no individual is to have complete control over any type of asset in any agency, department, or division of the state.

4. The Employment Security Department did not establish adequate controls over the Job Opportunities and Basic Skills Program.

Description of Condition

Our testing indicates there are inadequate controls over the Job Opportunities and Basic Skills (JOBS) federal program. ESD lacks adequate controls over JOBS program transactions initiated through the JOBS Financial System (JFS) and over documentation associated with these transactions. There are no safeguards in the JFS system to preclude an individual staff person from:

- Entering a fictitious vendor
- Entering a fictitious client
- Authorizing an inappropriate expenditure on a client's behalf
- Approving the payment
- Generating the warrant
- Deleting a vendor or client from JFS reports used for review of transactions
- Providing services to ineligible participants

We found no consistent compensating controls at the JOBS field offices we visited which would adequately address the weaknesses noted above. Instances were noted where one person was in a position to control all functions noted above. We found that:

- a. There was a lack of separation of duties at all seven JOBS offices audited. Individual staff members had control over all transaction processing, including adding vendors and initiating, approving and generating payments.
- b. The supervisory review of JOBS program transactions, vendor lists and participant eligibility was inadequate or non-existent at all seven offices audited.
- c. Controls over the supporting documentation of transportation payments at all offices audited were inadequate.
- d. Source documents for 66 payments, totaling \$7,679.43 were missing from four field offices. Additionally, numerous errors and miscalculations were noted.

Cause of Condition

ESD staff have indicated that in order to make JFS easy to use and thus streamline JOBS program operations, controls which would address the cited weaknesses within the JFS system were not developed. Compensating controls have not been developed at field office locations due to a lack of fixed responsibility for these duties within the agency and cutbacks in funding which removed the monitoring function at ESD. As a result, ESD did not fully implement prior planned corrective action or ensure that staff were adequately trained in supervisory review procedures and retention of payment documentation. These same conditions were reported in the *State of Washington Statewide Single Audit Report* for the fiscal years 1993, 1994, 1995 and 1996.

Effect of Condition

Lack of adequate controls could result in the occurrence of undetected errors and/or irregularities and unallowable costs to the JOBS program.

Recommendations

The agency should establish adequate controls and document procedures over the processing of JOBS program transactions through JFS and provide training to field staff on supervisory review procedures and retention of payment documentation.

Agency's Response

The agency has implemented the following corrective actions to improve controls over the JOBS Financial System (now used to process expenditures for the WorkFirst program):

1. *Each WorkFirst invoice will be reviewed by two individuals prior to payment. These individuals will sign the document evidencing their review and approval of the transaction.*
2. *Modifications have been made to the JOBS Financial System. System security has been changed so that only the supervisor model is authorized to add or update vendors on the vendor table. Only the Administrative model has authority to delete a vendor from the table. A monthly report listing all additions or updates to the*

vendor table will be available to each office for their review. Supervisors will no longer have the ability to input expenditure transactions to JFS.

3. *The Security Authorization Report maintained by the Office of Information Systems has been revised to reflect staff having access to the JOBS Financial System as well as the model they have been assigned. In addition, on a monthly basis, the central office WorkFirst Unit will mail each office the JFS Security Report showing staff with access for their review and action.*
4. *Training is being provided to all WorkFirst supervisors to clearly outline new procedures. This training is scheduled for completion by June 5, 1998. A desk aid will be provided at the time of training. The desk aid will provide a quick reference tool for program changes and required action steps for specific WorkFirst processes including: Invoice Voucher/Purchase Authorizations, Batch Handling, Vendor Payments, Cash Refunds and System Access/Security. The WorkFirst Supervisor Desk Aid and Vendor Payment Process Training will clearly address the importance of consistent WorkFirst procedures at all offices. The training will emphasize the importance of document/transaction reviews and the necessity for consistency to ensure accuracy and validity of each expenditure.*
5. *Thirty-eight of the 66 payments identified by the auditors have been located by the agency. Remaining outstanding vouchers total \$2,528.15. Additional research is planned for locating these vouchers.*
6. *With the advent of the WorkFirst program, ESD staff are no longer required to perform case manager services. During the training phase the need for staff to add clients to JAS (JOBS Automated System) will be evaluated. If this capability is no longer needed, it will be removed.*
7. *Post-employment services may be available to WorkFirst participants for up to twelve months after their grant is closed. System edits for post-employment services are currently being evaluated and should be in place by July 1, 1998.*

Auditor's Remarks

We appreciate the agency's efforts to resolve these weaknesses. We will review the corrective action during our next regular audit.

Applicable Laws and Regulations

The state of Washington Office of Financial Management's *Financial and Administrative Policies, Regulations, and Procedures* manual addresses basic principles of internal control at Section 6.1.1.2.4(b) which states, in part:

- (1) Division of Duties - Whenever possible no individual is to have complete control over any type of asset in any agency, department, or division of the state. The work of employees handling public assets should be complementary to or checked by other employees. This will not only decrease the chance of loss by means of fraud or dishonesty, but will also provide a means to detect errors.

(2) Sound Procedures and Policies - Every effort is to be made to ensure that the assets of the state are properly handled. By supplying employees with strict control procedures and ensuring that they are followed through the use of checks and audits, the chance of losses will be greatly decreased.